

October 14, 2008

**VIA ELECTRONIC DELIVERY**

**EX PARTE**

Ms. Marlene H. Dortch  
Secretary  
Federal Communications Commission  
Room TW-325  
445 12<sup>th</sup> Street, S.W.  
Washington D.C. 20554

**RE: CC Docket Nos. 01-92, 96-45; WC Docket Nos. 05-337, 99-68, 04-36**

Dear Ms Dortch:

The purpose of this letter is to (1) reiterate the joint proposal of tw telecom inc. (“TWTC”) and One Communications Corp. (“One”) for unified intercarrier compensation reform;<sup>1</sup> (2) respond to filings by AT&T,<sup>2</sup> Level 3,<sup>3</sup> Verizon,<sup>4</sup> and a group of carriers (which include AT&T and Verizon)

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<sup>1</sup> See Letter of Jonathan Lechter, Counsel, TWTC and One, to Marlene H. Dortch, Secretary, FCC, CC Dkt. Nos. 01-92 & 96-45, WC Dkt. Nos. 05-337 *et al* (filed Oct. 2, 2008). See also Comments of TWTC *et al.*, CC Dkt. No. 01-92 (filed May 23, 2005) (“TWTC 2005 Intercarrier Comp. Comments”). One Communications Corp. has become the parent entity of Conversent Communications, LLC, CTC Communications Corp., and Lightship Telecom, LLC, all of which were joint commenters with TWTC in earlier proceedings in this docket.

<sup>2</sup> See Letter of Gary L. Phillips, General Attorney and Associate General Counsel, AT&T, to Marlene H. Dortch, Secretary, FCC, CC Dkt. Nos. 01-92 *et al.* (filed May 9, 2008) (“AT&T ISP-Bound Letter”); Letter of Robert W. Quinn, Senior Vice President, Federal Regulatory, to Kevin J. Martin, Chairman, FCC, WC Dkt. Nos. 05-337 & 07-135, CC Dkt. Nos. 01-92 *et al.* (filed July 17, 2008) (“AT&T Comprehensive Reform Letter”). AT&T also filed a petition seeking “interim” intercarrier compensation reform in the event that that the FCC did not adopt its comprehensive reform proposals. See *Petition of AT&T Inc. for Interim Declaratory Ruling and Limited Waivers Regarding Access Charges and the “ESP Exemption,”* WC Dkt. No. 08-152 (filed July 23, 2008) (“AT&T Petition”). TWTC filed comments opposing portions of the petition. See TWTC Comments, WC Dkt. No. 08-152 (filed Aug. 21, 2008) (“TWTC AT&T Petition Comments”).

(“Carrier Group”)<sup>5</sup> regarding their respective approaches to intercarrier compensation reform; and (3) respond to AT&T’s and Verizon’s proposal for a numbers-based universal service contribution methodology.<sup>6</sup>

## 1. Introduction

It is clear that the existing intercarrier compensation system is unsustainable and in need of reform. It is no secret that the arbitrary application of different rates for the same transport and termination function depending on the nature of the traffic at issue creates inefficient incentives. But reforming this system is a complex undertaking that will have significant implications. Perhaps most importantly, intercarrier compensation reform will almost certainly cause carriers to recover a larger percentage of their costs from consumers who make few calls. Without more information, however, policy makers cannot know the magnitude of this increase or its effect on subscribership. Given the magnitude of these potential effects, the Commission must be sure that it understands whose rates will increase and by how much before approving a particular reform proposal. Thus far, insufficient information has been submitted in the record in this proceeding to make these assessments.

Moreover, the Commission should also examine closely the other risks associated with intercarrier compensation reform. For example, reducing and unifying terminating rates implicates proposals for a costly and inefficient Replacement Mechanism and substantial legal risks. If the FCC were simultaneously to attempt to reform the universal service contribution system, the process would become even more complex. The Commission’s apparent attempt to address all of these issues before the artificial deadline of November 5, 2008 (the deadline established by the D.C. Circuit for issuing rules governing the exchange of ISP-bound traffic) is imprudent and unnecessary. It would be far wiser for the Commission to resolve the ISP-bound traffic exchange issues by the court-set deadline and then proceed with addressing other reform issues in a deliberate fashion by a Further Notice of

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<sup>3</sup> See Letter of John T. Nakahata, Counsel, Level 3 Communications, LLC, CC Dkt. Nos. 99-68 & 01-92 (filed Aug. 18, 2008) (“*Level 3 Aug. 18 Letter*”).

<sup>4</sup> See Letter of Susan A. Guyer, Senior Vice President -- Federal Regulatory Affairs, Verizon, to Chairman Martin, Comm’r Copps, Comm’r McDowell, Comm’r Adelstein, and Comm’r Tate, CC Dkt. Nos. 01-92 & 96-45 (filed Sept. 12, 2008) (“*Verizon September 12 Letter*”); Verizon White Paper, attached to Letter of Donna Epps, Vice President, Federal Regulatory, Verizon, to Marlene H. Dortch, Secretary, FCC, CC Dkt. Nos. 01-92 & 96-45, WC Dkt. No. 04-36 (filed Sept. 19, 2008) (“*Verizon White Paper*”).

<sup>5</sup> See Letter of Verizon *et al.* to Chairman Martin, Comm’r Copps, Comm’r McDowell, Comm’r Adelstein, and Comm’r Tate, CC Dkt. No. 01-92, WC Dkt. No. 04-36 (filed Aug. 6, 2008) (“*Carrier Group Letter*”).

<sup>6</sup> See Letter of Mary L. Henze, AT&T, and Kathleen Grillo, Verizon, to Marlene H. Dortch, Secretary, FCC, WC Dkt. No. 06-122, CC Dkt. No. 96-45 (filed Sept. 11, 2008).

Proposed Rulemaking containing specific proposals and tentative conclusions, or other appropriate method.

Nevertheless, if the FCC insists on seeking to accomplish comprehensive intercarrier compensation reform by early November, it should do so in a manner that is both most efficient and least likely to be overturned on appeal. TWTC's and One's proposal that rates for the transport and termination of all traffic (including ISP-bound traffic) be set based on TELRIC meets these criteria. Under this approach, the FCC would continue to define, and if necessary refine, the pricing methodology used to set transport and termination rates, and states would implement that methodology by setting specific rates applicable to each incumbent LEC. The Commission could retain the rebuttable presumption that the rate applicable to Section 251(b)(5) traffic is "symmetrical," *i.e.*, that non-incumbent LECs' transport and termination rates equal the incumbent's in any particular area (*i.e.*, study area). *See* 47 C.F.R. § 51.711. As a result, all traffic terminated by any LEC in a study area would be subject to the same rate and all rates nationwide would be set pursuant to a uniform methodology.

As discussed below, this approach substantially reduces or avoids entirely several of the more vexing issues the Commission faces in its efforts to reform intercarrier compensation. For example, this approach is more likely to be sustained on appeal than the other major reform proposals. Setting rates based on TELRIC also obviates the need for a Replacement Mechanism for foregone intercarrier compensation revenues since cost-based rates would fully compensate incumbent LECs for the costs they incur when transporting and terminating traffic.

Finally, on the separate issue of the appropriate methodology for imposing universal service contribution obligations, the FCC should ensure that no reforms in this area cause substantial distortions in the marketplace. In particular, the FCC should reject a pure numbers-based scheme for universal service contributions, since that approach arbitrarily and dramatically punishes schools, universities, hospitals, government agencies, charitable organizations, and other end users that subscribe to services that require significant numbering resources, such as direct inward dialing numbers. At the same time, a pure numbers-based contribution system allows users of non-numbers-based interstate services, such as interstate interexchange services and private line data networks, to escape any contribution to universal service programs.

## **2. Establishing a National TELRIC-Based Methodology for Transport and Termination Rates is the Most Appropriate Means of Advancing the FCC's Objective of Eliminating the Inefficient Incentives Caused by the Existing Regime.**

The central problem with the existing intercarrier compensation regime is that each LEC charges different prices for terminating different kinds of traffic, even though the cost of the transport and termination function remains substantially the same. The joint proposal of TWTC and One Communications eliminates this problem while limiting or eliminating the problems associated with other reform proposals.

**a. The FCC Appears to Have the Authority to Require that Transport and Termination Rates for All Traffic Are Set in Accordance with a Uniform, Federally-Mandated Methodology.**

The Communications Act appears to grant the FCC the jurisdiction to require that rates charged by LECs to transport and terminate all traffic on their networks be set in accordance with an FCC-defined TELRIC methodology. In *AT&T v. Iowa Utils. Bd.*, 525 U.S. 366 (1999), the Supreme Court held that the FCC has the authority pursuant to Section 201(b) to adopt regulations implementing the terms of the Act. *See Iowa Utils. Bd.*, 525 U.S. at 378. In those instances, where a statutory provision encompasses both intrastate and interstate communications, the FCC may regulate both. *See id.* Section 251(b)(5), by its terms, encompasses the transport and termination of all “telecommunications”<sup>7</sup> regardless of jurisdiction, including intrastate access traffic.<sup>8</sup> Indeed, in the *ISP-Remand Order*, the FCC determined that Sections 251(b)(5) and Section 252(d)(2) cover *all* telecommunications traffic not excluded by section 251(g). Of course the FCC has the authority to remove categories of traffic from the purview of Section 251(g), causing the terms of Section 251(b)(5) and 252(d)(2) to apply. Some traffic, arguably including intrastate access traffic, has been subject to Section 251(b)(5) since the passage of the 1996 Act, but the FCC had not exercised its authority to expressly preempt the states. It appears that it has the authority to do so at any time. Finally, because the *WorldCom* court determined that ISP-bound traffic is not subject to Section 251(g), it must be subject to 251(b)(5) and the TELRIC-based pricing standard of Section 251(d)(2) (an issue that is discussed in greater detail below).

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<sup>7</sup> In addition, although the FCC has not yet determined whether voice traffic that originates in IP format qualifies as a telecommunications service, information service or as some other category of service, the FCC has held that VoIP providers offer “telecommunications.” *See Universal Service Contribution Methodology et al.*, Report and Order and Notice of Proposed Rulemaking, 21 FCC Rcd 7518 ¶ 35 (2006) (“[W]e find that interconnected VoIP providers are ‘providers of interstate telecommunications’ under section 254(d).”). Section 251(b)(5), which applies to all “telecommunications,” therefore applies to VoIP.

<sup>8</sup> Moreover, in determining that 251(b)(5) covers termination of traffic to a CMRS carrier, the FCC held that Section 251(b)(5) applies to traffic involving a LEC on only one end, and is not limited solely to calls involving a LEC on both ends of the call. *See Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, First Report and Order, 11 FCC Rcd 15499 ¶ 1041 (1996), *subsequent history omitted* (“*Local Competition Order*”) (“Although Section 252(b)(5) does not explicitly state to whom the LEC’s obligation runs, we find that LECs have a duty to establish reciprocal compensation arrangements with respect to local traffic originated by or terminating to any telecommunications carriers. CMRS providers are telecommunications carriers and, thus, LECs’ reciprocal compensation obligations under section 251(b)(5) apply to all local traffic transmitted between LECs and CMRS providers.”).

**b. TELRIC Yields Cost-Based Rates For Transport and Termination.**

Section 252(d)(2) states that the exchange rate for traffic subject to Section 251(b)(5) cannot be deemed just and reasonable unless such rate allows LECs to recover the “additional costs” of transport and termination. In the *Local Competition Order*, the FCC held that the traffic-sensitive portion of the TELRIC methodology constitutes the “additional cost” of transport and termination for purposes of Section 252(d)(2). The FCC determined that use of a network component causes a LEC to incur usage-sensitive costs if (1) the component of the network is shared or (2) there is an additional cost incurred by each increment of use, since capacity must eventually be increased to accommodate peak demand. If either of these criteria is met, the FCC has held that the incumbent LEC should recover its costs through usage-sensitive, per-minute rates. *Local Competition Order* ¶¶ 743-745. The Supreme Court subsequently held that TELRIC produces rates that are “just and reasonable” and do not inhibit investment.<sup>9</sup>

As TWTC, One and others have explained (*see, e.g., TWTC 2005 Inter-carrier Comp. Comments* at 10), the TELRIC-based method of calculating the “additional costs” of switching continues to be fundamentally sound. *First*, the capacity of switches is finite, and carriers purchase switches of different sizes depending on the traffic volumes that they anticipate will pass through the switch. BellSouth recently argued that, “[f]rom an economic standpoint, recovery of switch costs on a usage-sensitive basis is appropriate because those costs arise in a usage-sensitive manner.”<sup>10</sup> When a switch’s capacity is exhausted, it must be expanded. *See id.* Based on its own usage sensitive costs, BellSouth proposed establishing a unified end-office terminating rate of \$.00125, which it argues is similar to the TELRIC rates it proposed in state reciprocal compensation proceedings. *See id.* at 27. Similarly, USTA has argued that “switching capacity is never unlimited,” and “switching costs appear to be more variable with some soft switch deployments than with prior generations of switching technologies.”<sup>11</sup> *Second*, regardless of capacity, switches are shared facilities. Accordingly, based on FCC precedent, switching costs should continue to be recovered on a usage sensitive basis.

If anything, the proportion of usage-sensitive network costs associated with transport and termination on many networks may well be higher than is recognized by the TELRIC methodology. In the *Local Competition Order*, the FCC treated loop costs as non-usage sensitive because loop facilities were dedicated to a particular customer.<sup>12</sup> These costs were not considered part of the “additional costs” of transport and termination. However, carriers increasingly rely on shared loop

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<sup>9</sup> *See Verizon v. FCC*, 535 U.S. 467 (2002).

<sup>10</sup> BellSouth Corp. Comments, CC Dkt. No. 01-92, at 26 (filed May 23, 2005).

<sup>11</sup> *See USTA Comments*, CC Dkt. No. 01-92, at 24 (filed May 23, 2005).

<sup>12</sup> *See Local Competition Order* ¶ 1057 (“The costs of local loops and line ports associated with local switches do not vary in proportion to the number of calls terminated over these facilities. We conclude that non-traffic sensitive costs should not be considered ‘additional costs’ when a LEC terminates a call that originated on the network of a competing carrier.”).

facilities, such as fiber feeder loops. *See TWTC 2005 Intercarrier Comp. Comments* at 14. For example, most fiber-to-the-curb and fiber-to-the-premises architectures (like AT&T's U-Verse and Verizon's FiOS, respectively) currently being deployed utilize shared fiber feeder loop plant between the central office and a remote node. Similarly, usage-sensitive loop costs are a consistent feature of CMRS networks. As Sprint has shown, a large portion of a wireless carriers' costs are usage sensitive because both wireless switching infrastructure and wireless "loops" (*i.e.*, spectrum capacity) are shared among multiple subscribers.<sup>13</sup> Spectrum costs are also usage sensitive for the additional reason that, as carriers run out of spectrum capacity, they must acquire more spectrum, split cells or both. *See id.* at 13, 20. To the extent that existing TELRIC-based prices do not incorporate these shared costs, those rates may well be conservatively low.

In addition, it is appropriate to use the same methodology to set the rate for transporting and terminating all traffic. The FCC has repeatedly found that the costs a carrier incurs to perform transport and termination functions do not vary based on the nature or jurisdiction of the traffic involved.<sup>14</sup> This principle has been reaffirmed most recently by AT&T, among others.<sup>15</sup>

**c. TELRIC-Based Rates Will Eliminate Inefficient Incentives Created by the Existing Regime.**

Requiring that each LEC charges the same, cost-based rate for the transport and termination of all traffic would yield several fundamental policy benefits. *First*, carriers' incentive to invest in ways of misclassifying traffic to pay the lowest intercarrier rate or receive the highest intercarrier rate would

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<sup>13</sup> *See* Bridger M. Mitchell & Padmanabhan Srinagesh, *Transport and Termination Costs in PCS Networks: An Economic Analysis*, at 4 (Apr. 4, 2000) ("Spectrum and capacity in a BTS, a BSC, backhaul links, and MTX(s) are dedicated to a call for its duration. When the call is terminated, those resources are released and can be used to support another call."); *id.* at 10-11 ("To apply the Commission's rate standard in a wireless network, we inquire whether each component of a PCS network is shared by several users or whether it is dedicated to a single user. Next, we consider whether each component's costs are traffic-sensitive. Our analysis finds that handsets are resources dedicated to individual users and their costs are not traffic-sensitive, while all of the other components are shared among users of the wireless network and the costs of those elements are traffic sensitive.").

<sup>14</sup> *See, e.g., Implementation of the Local Competition Provisions in the Telecommunications Act of 1996; Intercarrier Compensation for ISP-Bound Traffic*, Order on Remand and Report & Order, 16 FCC Rcd 9151 n. 168 (2001) ("*ISP Remand Order*") ("We do not suggest that it costs CLECs less to serve ISPs than other types of customers.").

<sup>15</sup> *See* Letter of Henry Hultquist, Vice President, Federal Regulatory, AT&T, to Marlene H Dortch, Secretary, FCC, CC Dkt. Nos. 01-92 *et al.*, CC Dkt. Nos. 05-337 *et al.*, at 1 (July 17, 2008) (noting "the arbitrage opportunities created by the existing intercarrier compensation regime. That regime irrationally forces carriers to charge multiple rates for the performing the same basic functionality. It does so, moreover, based on obsolete regulatory distinctions that have been made untenable by today's converged broadband marketplace.").

disappear, since each LEC would charge the same rate for transporting and terminating all traffic. The elimination of this incentive would in turn obviate the need for the pending phantom traffic proceeding. *Second*, because the rates charged by LECs under this proposal would be cost-based, LECs would have no incentive to agree to artificially increase the volume of traffic that they transport and terminate. The elimination of this incentive would obviate the need for the pending traffic pumping proceeding. Accordingly, setting transport and termination rates based on TELRIC would eliminate the most harmful consequences of the existing regime.

**3. There Is No Legal or Policy Basis for the Adoption of Uniform National Rate of \$0.0007 for Transport and Termination of all Traffic.**

The FCC should reject the proposal that it adopt a single, national rate for the transport and termination of all traffic on all networks. This approach is far more likely to be overturned on appeal than the TELRIC-based approach proposed herein, and there is no cost basis for the proposed \$0.0007 rate.

**a. The FCC Does Not Have the Authority to Adopt a Uniform, National Terminating Rate.**

Section 2(b) of the Communications Act grants the states the authority to set rates for intrastate services, absent an express or implied grant to the FCC of such jurisdiction. *See* 47 U.S.C. § 152(b). As the FCC and the Supreme Court have determined, the Communications Act grants the FCC the authority to set pricing methodologies governing intrastate rates under Sections 251(b)(5) and 252(d)(2), but it does not grant the FCC the authority to set specific rates for intrastate services under those provisions.<sup>16</sup> Section 2(b) and Section 252(d)(2) reserve for the states the authority to set specific rates by implementing the pricing methodology established by the FCC. In fact, in *Iowa Utilities Board v. FCC*, the Eighth Circuit held that the FCC lacked the authority to set even an interim transport and termination rate (applicable from the release of the *Local Competition Order* to the conclusion of state TELRIC proceedings) for traffic subject to Section 251(b)(5).<sup>17</sup> The same logic

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<sup>16</sup> *See Local Competition Order* ¶ 29 (“The 1996 Act requires the states to set prices for interconnection and unbundled elements that are cost-based, nondiscriminatory, and may include a reasonable profit. To help the states accomplish this, the Commission concludes that the state commissions should set arbitrated rates for interconnection and access to unbundled elements pursuant to a forward-looking economic cost pricing methodology.”); *Iowa Utils. Bd.*, 525 U.S. at 384.

<sup>17</sup> *Iowa Utils. Bd. v. FCC*, 219 F.3d 744, 757 (8<sup>th</sup> Cir. 2000), *subsequent history omitted* (“[T]he FCC does not have the jurisdiction to set the actual prices for the state Commissions to use. Setting specific prices goes beyond the FCC’s authority to design a pricing methodology and intrudes on the states’ right to set the actual rates pursuant to § 252(c)(2)....We conclude that the proxy prices cannot stand and...vacate rules 51.513, 51.611 and 51.707.”).

renders unlawful the proposal that the FCC set a single, national intercarrier compensation rate of \$0.0007.<sup>18</sup> As explained below, Verizon's attempts to argue to the contrary are meritless.

**i. Impossibility Doctrine**

Verizon incorrectly asserts that the FCC may preempt intrastate access rates under the impossibility doctrine. *See generally Verizon White Paper*. Under that doctrine, the FCC may preempt state regulation of services that have an intrastate component if (1) it is impossible or impractical to separate the interstate and intrastate components of the service (the "inseverability" prong) and (2) the state regulation at issue would thwart or negate the implementation of a defined federal policy (the "purpose" prong).<sup>19</sup> Verizon argues that the inseverability prong is met because wireless and nomadic VoIP and similar services have now made it impossible to know whether any particular minute of traffic terminated by a carrier is interstate or intrastate in nature. *See Verizon White Paper* at 2. But this is not so.

In *Louisiana PSC v. FCC*, the Supreme Court rejected the application of the impossibility doctrine in a situation that closely resembles the instant context. In that case, the FCC argued that it could preempt state depreciation regulation because there was no way to know what portion of the equipment subject to such regulation was used to provide interstate versus intrastate service. The Court acknowledged that "the realities of technology and economics belie . . . a clean parceling of responsibility" between state and federal regulators of equipment costs for purposes of accounting rules.<sup>20</sup> Nevertheless, the Court held that the admittedly imprecise separations process provided a sufficient means of separating intrastate and interstate costs, thus foreclosing FCC preemption under the impossibility doctrine.

Just as accounting separations rules sufficed to distinguish costs assigned to the federal and state jurisdictions in *Louisiana PSC*, existing mechanisms such as the percentage interstate usage/percentage local usage ("PIU/PLU") studies suffice to distinguish traffic assigned to the federal and state jurisdictions for purposes of intercarrier compensation regulation. Indeed, as Verizon has explained in its phantom traffic comments, the jurisdiction of the vast majority of the traffic it receives from other carriers can be identified either through the use of traffic studies or other tools that have long been used by Verizon and other carriers. In opposing the new rule for phantom traffic proposed by the Missoula Plan, Verizon argued that what the "Missoula Plan supporters call 'phantom traffic' can, in fact, be billed using cost-effective tools that are available and widely used throughout the

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<sup>18</sup> As explained in more detail below, Level 3's proposal to set the ISP-bound rate at \$0.0007 and the AT&T proposal for Bill-and-Keep for ISP-bound traffic would face the same problems.

<sup>19</sup> *See Vonage Holding Corporation Petition for Declaratory Ruling Concerning an Order of the Minnesota Public Utils. Comm'n*, Memorandum Opinion and Order, 19 FCC Rcd 22404 ¶ 19 (2004) ("*Vonage Order*").

<sup>20</sup> *La. Public Serv. Comm'n v. FCC*, 476 U.S. 355, 360 (1996) ("*Louisiana PSC*").



industry today, including the use of billing factors set out in contracts and tariffs.”<sup>21</sup> Traffic whose jurisdiction cannot be identified immediately can be traced to the originating carrier in many instances through dedicated trunk groups (*see Verizon Phantom Traffic Comments* at 5) and jurisdiction can be ascertained “using a long-standing industry method known as ‘factoring’ to approximate the jurisdiction of the traffic received.” *Id.* at 7. Verizon uses factoring “to determine the jurisdiction of all wireless-originated calls, because for such calls the CPN will not necessarily reflect the geographic location of the calling party.” *Id.* at 8. Because of these tools, Verizon and other carriers are able to identify the jurisdiction of the vast majority of calls that they receive.

To be sure, there is a small percentage of traffic, primarily nomadic VoIP traffic, whose jurisdiction may not be identifiable. Even if this is true, the fact that a small portion of traffic cannot be identified does not give the FCC authority to preempt intrastate access charges for *all* traffic. As the FCC and the courts have found, preemption under the impossibility doctrine must be “narrowly tailored” to those circumstances where it is impossible to separate the subject of regulation between interstate and intrastate jurisdictions.<sup>22</sup> Accordingly, the FCC could, *at most*, preempt state regulation of traffic exchange arrangements involving the exchange of nomadic VoIP. All other traffic exchange arrangements would continue to be subject to dual federal-state regulation. Moreover, even application of the impossibility doctrine to nomadic VoIP is legally suspect. As AT&T has argued, there is no reason that the FCC should not and could not rely on calling numbers as a proxy for determining whether nomadic VoIP calls should be rated inter- or intrastate. *See AT&T Petition* at 33.<sup>23</sup>

Nor does the Vonage decision justify a different outcome. While in the *Vonage Order*, the FCC held that state entry and economic regulation of Vonage’s service should be preempted because of the multiple, simultaneous communications that occur during a VoIP communications session (*i.e.*, instant messaging using an interstate server), (*see Vonage Order* ¶ 25) this rationale does not apply to

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<sup>21</sup> *See Comments of Verizon on the Missoula Plan Phantom Traffic Proposal*, CC Dkt. No. 01-92 (Dec. 7, 2006) (“*Verizon Phantom Traffic Comments*”).

<sup>22</sup> For example, in *California I*, the court rejected the FCC’s argument that state structural separation requirements should be preempted because forcing a “carrier to separate its intrastate enhanced and basic services will necessarily force carriers to separate their interstate services as well, because the intra- and interstate components of enhanced services are structurally inseverable.” *California v. FCC*, 905 F.2d 1217, 1243-44 (9<sup>th</sup> Cir. 1990) (“*California I*”). The court found that preemption of *all* state separation requirements was not permitted because there were clearly identifiable intrastate enhanced services what could be distinguished from other mixed-jurisdiction enhanced services. *Id.* at 1244.

<sup>23</sup> AT&T argues that even though proxies could be used to determine whether traffic should be billed interstate or intrastate and that these proxies would be accurate in most cases, this has no bearing on the jurisdictional analysis. *See AT&T Petition* at 34 (“These mechanisms may be appropriate (though admittedly not perfect) for purposes of enabling a LEC to bill another carrier for intercarrier compensation.”). But AT&T provides no basis for this distinction and why the “imperfect” proxy of numbers is any different than the “imperfect” proxy of the separations rules in *Louisiana PSC*.

preemption of intrastate access charges to VoIP because the FCC only need to determine the jurisdiction of the *call* to assess access charges. Therefore, under the logic of *Louisiana PSC*, the FCC likely cannot preempt application of intrastate access charges to nomadic VoIP. But, even if it could, the FCC could not unify rates because the states would retain jurisdiction to impose intrastate access charges over the vast majority of traffic.

## **ii. Forbearance from Section 251(b)(5)**

Verizon next argues, again incorrectly, that the FCC could apply the uniform \$0.0007 terminating access rate to traffic currently subject to Section 251(b)(5) by forbearing from Section 251(b)(5) and applying the impossibility doctrine to that traffic as discussed above. *See Verizon White Paper* at 29. But, as also explained above, Section 2(b) of the Act grants the states the authority to regulate intrastate communications. The FCC may only preempt the states pursuant either to the impossibility doctrine (discussed above) or if the terms of the Communications Act (which the FCC may implement pursuant to Section 201(b)) encompass intrastate traffic. If the FCC were to forbear from 251(b)(5), it would eliminate the only provision in the Communications Act that encompasses the exchange of intrastate traffic. Absent that provision, regulatory authority over intrastate traffic would default to the states pursuant to Section 2(b). Rather than granting the FCC greater flexibility to regulate the exchange of intrastate traffic, forbearance from Section 251(b)(5) would eliminate entirely the basis for FCC jurisdiction.

## **iii. Additional Cost Standard in Section 252(d)(2)**

Verizon rather hopefully asserts that a national \$0.0007 rate comports with the “additional cost” standard in Section 252(d)(2)(A)(ii). Verizon makes three main arguments to support this theory, none of which have merit. *First*, Verizon argues that, because the FCC has found that a carrier incurs the same costs when terminating all traffic, the “additional costs” of all carriers could be met by a rate of \$.0007. *See Verizon White Paper* at 26-28. But while a LEC may recover the same transport and termination costs regardless of the traffic at issue, this does not mean that all LECs incur the same costs. Moreover, Verizon does not explain why mandating a \$0.0007 rate would not be impermissible rate-setting by the FCC.

*Second*, Verizon seems to argue that the FCC can directly preempt states from setting rates different than \$.0007 because the Supreme Court in *Iowa Utilities Board* held that “the 1996 Act establishes a ‘new federal regime...guided by federal-agency regulations’ and that a state commission must ‘regulat[e] in accordance with federal policy’ or a federal court ‘may bring it to heel.’” *Id.* at 27 (citing *Iowa Utils. Bd.*, 525 U.S. at 378 n.6). But the passage that Verizon cites in support of this assertion has nothing to do with whether the FCC may preempt state regulation in situations where, as is the case with Section 252(d)(2), states are granted the specific authority in a statute to set rates.<sup>24</sup>

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<sup>24</sup> *Iowa Utils. Bd.*, 525 U.S. at 378 (discussing unrelated issue raised by Justices Breyer and Thomas in dissent).

*Third*, Verizon argues that the FCC has the authority under Section 251(i) to ignore the specific grant of authority to the states in 252(d)(2) to set rates if, in exercising that authority, the states set rates that differ from the unified rate the FCC establishes for all other traffic. Verizon argues that, “if states were permitted, in implementing Section 251(b)(5) to set rates” at variance with the FCC’s unified rate, “such different rates would ‘affect the Commission’s authority under Section 201,’” contrary to Section 251(i). *Id.* at 28. But as explained in more detail below with respect to AT&T’s similar argument, Section 251(i) cannot be used as a bulldozer to eliminate the specific grants of authority to the states (*e.g.*, determining the meaning of “additional costs,” establishing UNE rates, etc.) in Section 252.

**b. \$0.0007 is Not Cost-Based.**

The proponents of the national \$0.0007 rate have barely even attempted to demonstrate that it is cost-based, and the little purported evidence provided to support this rate is utterly unreliable. In fact, Sprint is the only party to present empirical data attempting to show that \$.0007 meets the “additional costs” standard of Section 251(b)(5).<sup>25</sup> Based on its analysis of prices set pursuant to TELRIC by the states for unbundling switching and transport, Sprint argues that the national average rate for “switching” is \$0.00058 and that the national average rate for transport is \$0.00057. *See id.* at 3. Even Sprint’s analysis yields the conclusion that the combined rate for transport and termination is \$0.00115, far above \$0.0007. *See id.*

Furthermore, in performing this calculation, Sprint uses the rate for unbundled tandem switching as the rate for “termination.” *See id.* But end office termination is performed by end office, not tandem, switches. The rates for unbundled end office switching are generally substantially higher than the rate for unbundled tandem switching. Sprint’s arbitrary use of tandem switching rates therefore artificially lowers its national average.

In addition, a substantial percentage of the traffic subject to reciprocal compensation today is routed through *both* the tandem and end office switch. Even if it were reasonable to rely on the rate for unbundled tandem switching *in lieu* of the rate for end office switching, it would be necessary to include two switching charges (*i.e.*, two times the tandem switching rate) in the rate for a substantial percentage of the traffic. Sprint did not do that, thereby artificially lowering transport and termination rates yielded by application of the TELRIC methodology.

To provide the Commission with a more realistic estimate of the rates yielded by TELRIC, TWTC calculated the weighted average of the transport and termination rates it pays, including both those arrangements in which it interconnects with the incumbent LEC at the end office and those arrangements in which it interconnects at the tandem and pays two switching charges. This calculation yielded a weighted average of \$0.0023 per minute for reciprocal compensation that TWTC

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<sup>25</sup> *See* Ex Parte presentation, attached to Letter of Norina Moy, Director, Government Affairs, Sprint, to Marlene H. Dortch, Secretary, FCC, CC Dkt. No. 01-92 & WC Dkt. No. 04-36 (filed Sept. 26, 2008). Level 3 has tried to provide evidence in support of applying this rate to the exchange of ISP-bound traffic. That purported evidence is discussed separately below.

currently pays. In addition, as the chart attached hereto demonstrates, most of One Communications' operating companies' reciprocal compensation rates are far above \$0.0007.<sup>26</sup> Moreover, if the ILECs' past statements about TELRIC can be believed (and they are no less or more believable than their statements regarding the sufficiency of \$0.0007 in this proceeding), even rates yielded by TELRIC do not compensate ILECs for their network costs.<sup>27</sup>

**4. The Only Appropriate Means for LECs to Recover Foregone Intercarrier Compensation Revenue is Through Properly Regulated SLC Increases.**

Regardless of the manner in which the Commission reforms intercarrier compensation, local exchange carriers will experience reduced revenue from traffic exchange payments. The only appropriate means for LECs to compensate for these reduced revenues is through increases to end user rates, including properly regulated increased subscriber line charges ("SLCs").

**a. The FCC Should not Establish a Replacement Mechanism**

Verizon and AT&T have proposed that the FCC compensate local exchange carriers, apparently primarily incumbent LECs, for forgone intercarrier compensation revenue by allowing them to draw money from a Replacement Mechanism fund (presumably funded by the incumbent LECs' competitors). There is no basis for this proposal. Any cost-based rates for transport and termination (and, as explained, TELRIC-based rates qualify as cost based) fully compensate incumbent LECs for the transport and termination function. There is therefore no need for a Replacement Mechanism. Indeed, Verizon and AT&T do not even attempt to demonstrate that there is a cost basis for their Replacement Mechanism proposal. Rather, the proposal seems to be based on Verizon's and AT&T's conviction that it would be helpful if their competitors compensated them for foregone revenues, while protecting such revenue from competition.

Moreover, even if the FCC adopts a Replacement Mechanism, the fund should not support lines in those areas where local end-user rates have been deregulated. The underlying rationale for recovering a portion of the lost access revenue through "subsidy" payments instead of end-user rates (SLCs or intrastate rates for phone service) is that end-user recovery might, in higher cost areas, cause telephone service to become unaffordable. But in areas where intrastate prices have been completely deregulated already, the state commission has made a determination that competition will ensure that rates are driven towards cost. In addition, ILEC-only USF payments will be particularly damaging to competition in those areas where rates have been deregulated and competition is highest because ILECs will use their subsidy payments to drive out competitors. Accordingly, in areas where incumbent LEC local rates have been deregulated, subsidies are unnecessary and affirmatively harmful.

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<sup>26</sup> See Attachment A attached hereto. One Communications was unable to obtain the information needed to perform a weighted average calculation.

<sup>27</sup> See generally *Verizon v. FCC*, 535 U.S. 467 (2002) (where ILECs challenged TELRIC as providing less than "just and reasonable" compensation).

The Commission should also make sure that the Replacement Mechanism accounts for the high per-line revenues ILECs earn when selling voice service bundled with broadband and/or video service. This can be achieved in one of two ways. The Commission could set the per line revenue benchmark at the national average per-line price for telephone service and then compare that benchmark to the revenue an ILEC earns from all services, including broadband and video, provided over the line. If the total revenues associated with the line exceed the benchmark, no Replacement Mechanism payment would apply to that line. Alternatively, if the Commission were to adopt the structure proposed by AT&T and Verizon (under which the Replacement Mechanism covers the access shift to the extent it cannot be recovered from end user rates set at an average National Comparability Benchmark), then the benchmark should account for the fact that ILECs earn revenue from many services provided over their end user connections other than local telephone service. As Sprint has argued, this means that the National Comparability Benchmark should either be set at or around \$60, to account for revenues associated with bundled offerings of local telephone service and other services. If the National Comparability Benchmark is set at the average revenue associated with stand-alone local telephone service, then a proportion of the costs of the network attributable to other services, such as broadband and video, must be excluded from the total costs to be recovered via the Replacement Mechanism.<sup>28</sup>

Finally, the FCC should reject Verizon's proposal that "when [a] LEC experiences a decline in access lines, the support associated with those lost lines phases out over three years, in equal increments."<sup>29</sup> Verizon has not shown how or why per-line costs would remain after it loses a line. Even the Missoula Plan did not propose such a sop to ILECs.<sup>30</sup> To the extent that the loss in access minutes per line is attributable to the ILECs' own wireless subsidiaries or broadband offering (by increased use of e-mail in lieu of voice communications), the ILECs obtain a double recovery. In this regard, Verizon's proposal is particularly nonsensical.

**b. Incumbent LECs should be Permitted to Recover Foregone Inter-carrier Compensation Revenue Only from Appropriately Regulated SLC Increases.**

Both AT&T and Verizon also propose permitting carriers to increase their SLCs to make up for lost access revenue. *See AT&T Comprehensive Reform Letter* at 7; *Verizon Plan* at 6. While

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<sup>28</sup> See Letter from Anna Gomez, Sprint Nextel Corporation, to Marlene H. Dortch, Secretary, FCC, CC Docket Nos. 01-92 & 96-45, WC Dkt. No. 04-36 (filed Oct. 8, 2008).

<sup>29</sup> See *Verizon Proposal for Inter-carrier Compensation Reform*, attached to *Verizon September 12 Letter*, at 8 ("Verizon Plan").

<sup>30</sup> See *Missoula Inter-carrier Compensation Plan*, attached to Letter from Tony Clark, Commissioner & Chair, NARUC Comm'n on Telecommunications; Ray Baum, Commissioner & Chair, NARUC Task Force; and Lary Landis, Commissioner & Vice-Chair, NARUC Task Force, to Marlene H. Dortch, Secretary, FCC, CC Dkt. No. 01-92, at 68 (filed July 24, 2006) ("*Missoula Plan*") ("Because recovery from the Restructure Mechanism is calculated on a *per-line basis*, the loss of a line at any Step of the Plan will result in a loss of Restructure Mechanism dollars.") (emphasis in original).

TWTC and One agree that ILECs should be permitted to have the *opportunity* to recover their lost intercarrier revenues through either SLCs or increased state-regulated end-user rates, their proposals for SLC increases would permit ILECs to engage in anticompetitive cross-subsidy. As TWTC explained in response to AT&T's recent "interim" intercarrier compensation reform petition (*see TWTC AT&T Petition Comments*), the Missoula Plan,<sup>31</sup> and the 2005 *Inter-carrier Compensation FNPRM*,<sup>32</sup> safeguards should be established to ensure that ILECs cannot subsidize higher end-user rates or SLCs in product markets and geographic markets subject to more competition (e.g., enterprise market and urban markets) with higher SLCs in areas subject to less competition (e.g., mass market and rural markets). As TWTC explained in response to AT&T's petition, the current SLC deaveraging rules do not prevent such cross-subsidies. *See TWTC AT&T Petition Comments* at 12.

Accordingly, if the FCC chooses to permit ILECs to increase their SLCs to cover lost intercarrier revenue, the FCC should ensure that ILECs recover lost intercarrier payments through SLC increases by customer class in proportion to the extent that intercarrier payments are lost by customer class. That is, losses incurred in multiline business terminating access revenues should be recouped by increasing (wherever competitive circumstances permit) multiline business SLCs, and, similarly, losses in residential line terminating revenues should be recovered by increasing the residential line SLCs. The FCC should also ensure that incumbent LECs are not permitted to recover lost intercarrier revenues by selectively raising SLCs in geographic areas with little or no competition, while lowering them in areas subject to greater competition. *See id.*

## **5. Tandem Transit Rates Should be Subject to the Same Level of Rate Regulation as Transport and Termination.**

Verizon inexplicably argues that tandem transit rates set forth in interconnection agreements or tariffs should be capped at interstate access rate levels, which are substantially higher than \$0.0007 or TELRIC-based rates.<sup>33</sup> Verizon suggests further that the FCC remove all regulation of tandem transit rates by 2010.<sup>34</sup> Verizon provides no justification for treating tandem transit traffic differently than

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<sup>31</sup> Comments of TWTC *et al.*, CC Dkt. No. 01-92, at 14 (Oct. 25, 2006) ("*TWTC Missoula Plan Comments*") ("The Commission must not allow the incumbents to recover intercarrier compensation revenue currently associated with one product or geographic market from another product or geographic market.").

<sup>32</sup> *TWTC 2005 Inter-carrier Comp. Comments* at 41 ("Most fundamentally, the Commission must not allow incumbents to recover intercarrier compensation revenue currently associated with multi-line business customers (for whom there are competitive alternatives) from mass market customers.").

<sup>33</sup> *See Verizon Plan* at 4 ("At the outset of the plan, existing rates for tandem transit service subject to agreements or local interconnection tariffs will remain in effect. Rates for tandem transit service subject to access tariffs will be capped at today's interstate access rates.").

<sup>34</sup> *See id.* ("The Commission will issue a Further Notice of Proposed Rulemaking to consider, among other things, the competitive circumstances under which the cap on the tandem transit service rate may

other intercarrier compensation traffic. Nor could it. Tandem switching involves the exact same functionality and causes carriers to incur the exact same costs when used to transmit access, reciprocal compensation and transit traffic. The real reason that Verizon wants rates for tandem transit to remain deregulated is that, as the FCC has recognized, incumbent LECs retain a virtual monopoly over the provision of those services and they would be uniquely advantaged by deregulated rates.<sup>35</sup> The Commission must not offer incumbent LECs the opportunity to raise rivals' costs by abusing their market power over tandem switching service. It should therefore require that incumbent LECs tariff their tandem transit service at TELRIC-based rate levels.

## **6. There is no Basis for Changing Regulations Governing Network Interconnection Architecture.**

Verizon also resurrects elements of the "edge" interconnection architecture proposal first put forth as part of the ICF plan and later included in the Missoula Plan. *See Verizon Plan* at 1-2. AT&T similarly seems to have recently met with the FCC to again advocate some version of the edge plan as well.<sup>36</sup> As TWTC explained most recently in its comments on the *Missoula Plan*, changes in interconnection architecture would substantially increase CLECs' costs and violate the CLECs' rights to interconnect with ILECs' networks at any technically feasible point. *See TWTC Missoula Plan Comments* at 16-19. These criticisms apply equally to Verizon's proposal.<sup>37</sup> More importantly, regardless of the merits of any interconnection architecture proposal, adoption of such a change is not a prerequisite to the accomplishment of the FCC's main goal in this proceeding: unifying intercarrier compensation rates.

## **7. The Protections of Sections 251 and 252 Must Apply to Agreements Implementing New Intercarrier Compensation Rules.**

Verizon argues that, while the FCC should adopt the detailed rules presented in its plan, these rules "should be a default regime only" and "[p]roviders should be permitted – indeed, encouraged – to enter into alternative commercial arrangements." *Verizon September 12 Letter* at 3. Nevertheless, the statute mandates that agreements regarding rights encompassed by Section 251 *must* continue to be

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be modified or eliminated. The Commission should complete its rulemaking and adopt final transit rules by December 31, 2009.").

<sup>35</sup> *See Developing a Unified Intercarrier Compensation Regime*, Notice of Proposed Rulemaking, 16 FCC Rcd 9610 ¶ 125 (2001) ("*Intercarrier Compensation Regime NPRM*").

<sup>36</sup> *See, e.g.,* AT&T's Presentation "*The Path to a Broadband Future - Unified Terminating Rates*," attached to Letter of Brian Benison, Director, Federal Regulatory, AT&T, to Marlene H. Dortch, Secretary, FCC, CC Dkt. Nos. 01-92 *et al.*, CC Dkt. Nos. 05-337 *et al.* (filed Sept. 12, 2008).

<sup>37</sup> *See Ex Parte* Letter of Steven F. Morris, Associate General Counsel, NCTA, on behalf of NCTA and COMPTTEL, to Marlene H. Dortch, Secretary, FCC, WC Dkt. Nos. 01-92 *et al.*, at 2 (filed Oct. 1, 2008).

subject to the protections of Sections 251(b) and 251(c) and such agreements must be filed with state commissions subject to the full panoply of Section 252 requirements, including state arbitration, “opt - in” rights under Section 252(i) and so forth.<sup>38</sup> Congress’s intent in imposing a duty on ILECs to interconnect as well as the other provisions of Section 251 was to ensure that ILECs do not act on their incentive to leverage their market power in the local exchange market to disadvantage competitors. Because ILECs still retain such leverage, they must not be permitted to cut secret agreements or wiggle out of their duties under the statute. While Verizon has recently stated that it now agrees that the provisions of Sections 251 and 252 should apply to agreements reached pursuant to its plan, the Commission should leave no doubt about the matter by expressly mandating this result.<sup>39</sup>

## **8. The Commission Must Ensure That Its Universal Service Contribution Methodology Does Not Arbitrarily Harm Certain Types of End Users.**

Verizon and AT&T recently proposed an ill-advised plan to change the FCC’s USF contribution methodology from revenue-based to numbers-based. This proposal is not new. The FCC sought comment on a nearly identical plan five years ago.<sup>40</sup> Verizon’s and AT&T’s plan suffers from the same fundamental problem as that staff plan on which the FCC sought comment: it would place an inappropriate burden on those customers that rely heavily on numbering resources such as universities, hospitals, and government agencies. As TWTC argued previously, a numbers-based scheme would (1) exclude from the pool of contributions interexchange services in violation of Section 254(d) that “every” provider of interstate telecommunications service contributes “on an equitable and nondiscriminatory basis;” (2) exclude stand-alone broadband and private line data services from fund contribution obligations; and (3) make up for these losses by imposing large contribution obligations on number-intensive services (*e.g.*, DID based services).<sup>41</sup>

The AT&T/Verizon plan would fall particularly hard on purchasers of channelized voice service to businesses. *See TWTC 2003 Reply Comments* at 12. Based on TWTC’s own estimates, its USF contribution obligation (which it generally passes through to end user customers) would increase 148 percent overall as compared to the current revenues-based system. Customers that use large

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<sup>38</sup> *Cf. Local Competition Order* ¶ 118 (“States must comply with both the statutory standards under section 252(d) *and* the regulations prescribed by the Commission pursuant to section 251 when arbitrating rate disputes or when reviewing BOC statements of generally available terms. Section 252(c) enumerates three requirements that states must follow in arbitrating issues. These requirements are not set forth in the alternative; rather, states must comply with all three.”) (emphasis added).

<sup>39</sup> *See* Letter of Donna Epps, Vice President, Federal Regulatory, Verizon, to Marlene H. Dortch, Secretary, FCC, CC Dkt. Nos. 01-92 *et al.*, (filed Oct. 3, 2008).

<sup>40</sup> *See Commission Seeks Comment on Staff Study of Alternative Contribution Methodologies*, Public Notice, 18 FCC Rcd 3006 (2003).

<sup>41</sup> *See TWTC Reply Comments*, CC Dkt. Nos. 96-45 *et al.* (filed Apr. 18, 2003) (“*TWTC 2003 Reply Comments*”).



blocks of numbers such as universities, hospitals and government agencies, would experience increases far in excess of 148 percent. For example, a switch to a pure numbers-based contribution system would cause TWTC's government agency customers to experience on average a 1032 percent increase in contribution obligations, its hospital customers to experience on average a 3124 percent increase, its schools/university customers to experience on average a 2421 percent increase, and its charitable organization customers to experience on average a 469 percent increase. Such increases could have a substantial, real-world effect on individual customers. For example, the annual universal service contribution obligation associated with one of TWTC's hospital customers is currently \$1,757, but that would increase to \$271,320 under a pure numbers-based approach. This kind of increase can be devastating for financially strapped hospitals. Similarly, the annual universal service contribution obligation associated with one of TWTC's university customers is currently \$4,082, but that would increase to \$418,932 under a pure numbers-based approach. Again, this kind of cost increase would be extraordinarily burdensome for government agencies that already face growing budget deficits. To address this problem, the FCC should adopt some combination of a numbers-based and connection-based scheme (based on capacity) that also ensures that stand-alone long-distance providers contribute to the fund.

But even if a numbers-based scheme made sense from a theoretical standpoint, AT&T's and Verizon's plan must be rejected because they do not quantify, even in the most rudimentary way, the impact of their plan. In 2003, the staff rigorously modeled the impact of three different contribution proposals, including a numbers-based scheme. Those models are of little utility in evaluating the AT&T/Verizon plan because so much has changed since then, including the wireless safe harbor, the volume of numbers in service, and the inclusion of VoIP service revenues in the contribution base. Nor does either AT&T or Verizon model the impact of their proposed increases in the universal service fund that would result from a broadband fund and a Replacement Mechanism. The FCC must not undertake major policy changes such as the ones Verizon and AT&T propose without sufficient empirical analysis.

**9. There is no Basis for Setting the Rate for the Exchange of ISP-Bound Traffic at Bill and Keep or at \$.0007.**

ISP-bound traffic must be treated like all other traffic for purposes of setting the applicable transport and termination rates. AT&T's and Level 3's arguments to the contrary are meritless.

**a. Section 201(i) May Not be Read to Eviscerate Sections 251(b)(5) and 252(d)(2).**

AT&T argues that ISP-bound traffic need not be subject to Section 251(b)(5) and the pricing standard of Section 252(d)(2), because the "savings clause" of Section 251(i)<sup>42</sup> permits the FCC to set the price for ISP-bound traffic pursuant to its general authority under Section 201. There is no merit to this argument. *See AT&T ISP-Bound Letter* at 2-4.

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<sup>42</sup> *See* 47 U.S.C. § 251(i)--Savings Provision.--"Nothing in this section shall be construed to limit or otherwise affect the Commission's authority under Section 201.

To begin with, as AT&T acknowledges, a savings clause such as Section 251(i) “cannot preserve rights that would be inconsistent with the Act itself.” *See id.* at 4. The basic rule is, as AT&T notes, that “courts disfavor aggressive readings of savings clauses that would cause a statute to ‘destroy itself’ by canceling out its own provisions.”<sup>43</sup> AT&T’s interpretation of Section 251(i) would in fact “destroy” the rest of Section 251. While Section 251(i) might permit the FCC to set ISP-bound rates pursuant to its general authority under Section 201 *if there were not a specific provision in Section 251 covering that traffic*, the specific (Section 251(b)(5) and the pricing clause of Section 252(d)(2)) must trump the general reservation of authority to the FCC in Section 201.<sup>44</sup> Congress could not have intended to allow the FCC to simply invoke its Section 201 authority to ignore the specific provisions of Sections 251 and 252. Under AT&T’s interpretation, the FCC could set any rate that it wants for UNEs used to provide interstate service (or an inseverable mix of interstate and intrastate services) or it could take away states’ jurisdiction to adjudicate interconnection disputes. This was plainly not Congress’ intent.<sup>45</sup>

Moreover, AT&T’s approach is not the only interpretation of Section 251(i) that would prevent that provision from becoming a “waste of ink,” as AT&T alleges. *See AT&T ISP-Bound Letter* at 4. Section 251(i) does have a clear purpose: to ensure that Section 251 is not interpreted to eliminate the FCC’s authority to regulate interstate matters not otherwise covered by the express provisions of Section 251. As the FCC clearly stated in the *Local Competition Order*, section 251(i) “merely affirms that the Commission’s preexisting authority under Section 201 continues to apply for purely interstate activities. It does not act as a limitation on the agency’s authority under section 251.” *Local Competition Order* ¶ 91.

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<sup>43</sup> *See id.* at 4; *see also Am. Tel. & Tel. Co. v. Central Office Tel.*, 524 U.S. 214, 227 (1998) (“The savings clause of the Communications Act, § 414, contrary to respondent’s reading of it, does not dictate a different result....[The savings clause] preserves only those rights that are *not inconsistent with* the statutory filed-tariff requirements. A claim for services that constitute unlawful preferences or that directly conflict with the tariff -- the basis for both the tort and contract claims here -- cannot be ‘saved’ under § 414....The savings clause...cannot in reason be construed as continuing [a] common law right, the continued existence of which would be absolutely inconsistent with the provisions of the act. In other words, the act cannot be held to destroy itself.”) (emphasis added; internal cites omitted); *United States v. Locke*, 529 U.S. 89, 106 (2000) (stating the court’s policy to “decline to give broad effect to saving clauses where doing so would upset the careful regulatory scheme established by federal law.”).

<sup>44</sup> *Varity Corp. v. Howe*, 516 U.S. 489, 522 (1996) (observing the canon of statutory construction “that *specific enactments trump general ones* in carefully constructed statutes.”) (emphasis added).

<sup>45</sup> As the Supreme Court held, the Act establishes “a scheme in which Congress has broadly extended its law into the field of intrastate communications, but in a few specified areas (ratemaking, interconnection agreements, etc.) has left the policy implications of that extension to be determined by state commissions, [and those decisions] are beyond federal control....[The FCC may only] “issue[] rules to [guide the state-commission judgments].” *See Iowa Utils Bd.*, 525 U.S. at 385 & n.10.

AT&T is also incorrect that the FCC adopted AT&T's view of Section 251(i) in the *ISP Remand Order*. Through misleading use of ellipsis, AT&T selectively quotes from the *ISP Remand Order* to make it seem as though the FCC believed that Section 251(i) permits the Commission to set any rate for traffic that would normally fall under Section 251(b)(5) pursuant to Section 201. But AT&T's quote omits the FCC's holding (later overturned on appeal by *WorldCom*) that ISP-bound traffic was not subject to Section 251(b)(5) *because it was subject to the pre-Act rate regime under Section 251(g)*.<sup>46</sup> It is likely that the FCC could set the rate for ISP-bound traffic pursuant to Section 201 and the savings clause of Section 251(i) if ISP-bound traffic fell under the pre-Act obligations listed in Section 251(g) (and therefore Section 251(b)(5) would not apply). But because the D.C. Circuit determined in *WorldCom* that ISP-bound traffic does not fall within Section 251(g), the specific mandates of Section 251(b)(5) and 252 must apply to ISP-bound traffic.

**b. Setting ISP-Bound Rates at Zero is Inconsistent with the FCC's Conclusions Regarding the Sufficiency of End-User Rates Paid by ISPs.**

AT&T argues that Section 251(g) "preserves" the ESP access charge exemption and the only way that the Commission can "maintain the integrity of that regime" is to set ISP-bound traffic rates pursuant to Section 201 at Bill and Keep (*i.e.*, zero). *See AT&T ISP-Bound Letter* at 4. This argument also fails.

As an initial matter, AT&T does not cite to a court or FCC decision in support of the notion that Section 251(g) "preserved" the ESP exemption. This is unsurprising as the ESP exemption is an *exemption* (or a right) that applies to non-carriers (ESPs) while section 251(g) concerns *duties*

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<sup>46</sup> Compare *AT&T ISP-Bound Letter* at 3 (citing *ISP Remand Order*) ("In the ISP Recip. Comp. Remand Order, the Commission explained: 'subsection (i) ensures that, on a going forward basis, the Commission has the authority to establish pricing for, and otherwise to regulate, interstate access services... Thus, subsection (i) expressly affirms the Commission's role in an evolving telecommunications marketplace, in which Congress anticipates that the Commission will continue to develop appropriate pricing and compensation mechanisms for traffic that falls within the purview of section 201.'" with *ISP Remand Order* ¶¶ 49-50 ("When read as a whole, the most natural reading of section 251 is as follows: subsection (b) sets forth reciprocal compensation requirements for the transport and termination of "telecommunications"; subsection (g) *excludes certain access services (including ISP-bound traffic) from that requirement*; and subsection (i) ensures that, on a going-forward basis, the Commission has the authority to establish pricing for, and otherwise to regulate, interstate access services. When viewed in the overall context of section 251, subsections (g) and (i) serve compatible, but different, purposes. Subsection (g) *preserves rules and regulations that existed at the time Congress passed the 1996 Act, and thus functions primarily as a 'backward-looking' provision* (although it does grant the Commission the authority to supersede existing regulations). In contrast, we interpret section 251(i) to be a 'forward-looking' provision. Thus, subsection (i) expressly affirms the Commission's role in an evolving telecommunications marketplace....) (emphasis added).

imposed upon “each local exchange carrier.”<sup>47</sup> More importantly, AT&T’s position seems to rest entirely on its *policy arguments* that (1) intercarrier payments are unnecessary and would permit double recovery for ISP bound traffic, and (2) if the ESP exemption did not apply, the two LECs that originate and terminate a call to the ESP would actually be jointly providing access services to an IXC (*i.e.*, the ESP). *AT&T ISP-Bound Letter* at 5. AT&T obviously would prefer not to pay LECs serving ISPs to perform a termination function, but there is no basis for its preference in law or policy.

AT&T offers no legal or factual support for its claim that the FCC has found that the end-user rates that LECs charge ISPs for local business lines “fully cover[] the cost of an ISP-serving LEC.” In fact, AT&T contradicts itself *later in the same paragraph* of its filing when it asserts that ILECs “complained to the Commission that they were *not* fully recovering their costs of call termination” to ISPs.” See *AT&T ISP-Bound Letter* at 5 (emphasis added). Either end-user rates fully compensate LECs for their costs or they do not. If they do not, then intercarrier payments would not constitute double recovery as AT&T alleges.

In any case, AT&T substantially distorts the FCC’s finding in the *1997 Access Charge Order*. The FCC never suggested in that order that, when a carrier only serves the ISP (and not the ISP subscriber as well), it should recover its costs from its own end-users. In the paragraph cited by AT&T, the FCC held that an ILEC serving *both ends* of an ISP-bound call is compensated by both end-user rates and *other sources of revenue* that would be unavailable to carriers that served only the ISP (*e.g.*, charges for second lines and fees for internet access services).<sup>48</sup> More fundamentally, because the same carrier (the ILEC) served both ends of the call in the scenario described in the *1997 Access Charge Order*, there could not be any intercarrier payments between LECs; the ILEC would have no choice but to recover any terminating costs through end-user charges. In addition, contrary to AT&T’s assertion, the FCC did not tell carriers that they could address their revenue shortfall by “raising the rates they charged their ISP customers pursuant to the ESP exemption rate structure.” *AT&T ISP-Bound Letter* at 5. Rather, the FCC merely said that carriers could “address their concerns to state regulators.” *1997 Access Charge Order* ¶ 346. This could have meant that ILECs could ask

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<sup>47</sup> See 47 U.S.C. § 251(g) (“On and after February 8, 1996, each local exchange carrier, to the extent that it provides wireline services, shall provide exchange access, information access, and exchange services for such access to interexchange carrier and information service providers in the same equal access and non-discriminatory interconnection restrictions and obligations (including receipt of compensation) that apply to such carrier on the date immediately preceding February 8, 1996.”).

<sup>48</sup> See *Access Charge Reform et al.*, First Report and Order, 12 FCC Rcd 15982, ¶ 346 (1997) (“*1997 Access Charge Order*”) (“We also are not convinced that the nonassessment of access charges results in ISPs imposing uncompensated costs on incumbent LECs. ISPs do pay for their connections to incumbent LEC networks by purchasing services under state tariffs. Incumbent LECs also receive incremental revenue from Internet usage through higher demand for second lines by consumers, usage of dedicated data lines by ISPs, and subscriptions to incumbent LEC Internet access services. To the extent that some intrastate rate structures fail to compensate incumbent LECs adequately for providing service to customers with high volumes of incoming calls, incumbent LECs may address their concerns to state regulators.”).

for increased rates paid by ISP subscribers. Indeed, this is a reasonable interpretation given that the FCC believed that ILECs could be made whole at least in part by charges for second lines and internet access imposed on the customer originating the call.

AT&T also cites to paragraph 88 of *ISP-Remand Order* to support its assertion that intercarrier payments would result in double recovery. In that paragraph, the FCC justified its lower rate for ISP-bound traffic based on its finding that it “was not convinced” that originating carriers’ end-user rates “are designed to recover from the originating end-user the costs of delivering calls to ISPs.” *ISP Remand Order* ¶ 88. But the FCC never explained why originating carriers’ end-user rates *did* cover the costs of termination for voice traffic (justifying a higher intercarrier TELRIC-based rate). As explained, traffic termination imposes the same costs on LECs regardless of the nature of the traffic terminated. ILECs also charge the same end-user rates regardless of the nature of the traffic terminated (*e.g.*, a business or an ISP both pay the same rate for a PRI circuit regardless of whether the circuit carries voice or data traffic).<sup>49</sup> There is therefore no basis for AT&T’s assertion that the FCC has found that end-user rates fully compensate carriers serving ISPs, but not carriers serving other customers.<sup>50</sup>

In any event, even if Section 251(g) “preserved” the ESP exemption and AT&T is correct that, for *policy reasons*, it would make sense to set an ISP-bound traffic rate of zero to “maintain the integrity” of the ESP exemption, these facts cannot prevent the application of Sections 251(b)(5) and 252(d) to ISP-bound traffic. As the *WorldCom* court held, policy goals cannot trump the clear commands of the statute. In the *ISP Remand Order*, the FCC sought to place ISP-bound traffic outside of the ambit of Section 251(b)(5) in part because it believed that the rules adopted, such as the mirroring rule, would limit perceived arbitrage opportunities. *See ISP Remand Order* ¶ 21. The *WorldCom* court did not even examine this policy rationale, merely holding that ISP-bound traffic did not fall under the ambit of Section 251(g).<sup>51</sup>

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<sup>49</sup> See AT&T Enterprise, *Primary Rate ISDN (PRI)*, at [http://www.business.att.com/enterprise/Service/no\\_serv/no\\_fam/isdnpri\\_svcdetvaryingcontent/state=Ohio/](http://www.business.att.com/enterprise/Service/no_serv/no_fam/isdnpri_svcdetvaryingcontent/state=Ohio/) (explaining that AT&T’s PRI service “can be used for virtually any combination of voice, video, or switched data transmissions. There is no need to designate certain channels for each type of transmission; your bandwidth is allocated automatically for each transmission on a call-by-call basis.”).

<sup>50</sup> See also Declaration of Lee Selwyn, attached to Comments of Pac-West, WC Dkt. No. 08-152, ¶¶ 20-26 (Aug. 21, 2008).

<sup>51</sup> The court found that “[h]aving found that § 251(g) does not provide a basis for the Commission’s action, we make no further determinations.” *WorldCom, Inc. v. FCC*, 288 F.3d 429, 434 (D.C. Cir. 2002).

**c. The FCC May Not Mandate Bill-and-Keep for ISP-Bound Traffic Pursuant to Section 251(b)(5).**

AT&T argues that even if ISP-bound traffic is subject to Section 251(b)(5), the FCC may mandate bill-and-keep for such traffic. But AT&T is incorrect because ISP-bound traffic is always out of balance and a rate of zero constitutes direct FCC ratemaking. *See AT&T ISP-Bound Letter* at 6-7.

The FCC has already held that it may not impose bill-and-keep for out-of-balance traffic subject to Section 251(b)(5). The FCC found in the *Local Competition Order* that a LEC would be denied its statutory right to “mutual and reciprocal” recovery of costs under a bill-and-keep regime if it terminated more traffic than it originated (assuming that both carriers have the same transport and termination costs). This is because the carrier terminating more traffic would be unable to recover its costs from the *other carrier*.<sup>52</sup> AT&T believes that this finding is not mandated by the statute because (1) “Section 252(d)(2)(B)(i) permits . . . any compensation regime that ‘waive[s] the mutual recovery of costs,’” and the FCC can *mandate* that carriers “waive” mutual recovery of costs and (2) carriers need not cover their “mutual and reciprocal” costs from another carrier, but may recover these costs from their own end users. *See AT&T ISP-Bound Letter* at 7. But AT&T is incorrect on both of these points.

*First*, it is hard to understand how the FCC could *mandate* that carriers “waive” their rights to recovery from other carriers. Only the party that possesses a right may “waive” that right. Indeed, Merriam-Webster Dictionary defines “waive” as “to relinquish *voluntarily*” (emphasis added) or “to refrain from pressing or enforcing (as a claim or rule).”<sup>53</sup> There is nothing “voluntary” about the FCC commanding that a carrier adopt bill-and-keep. *Second*, the statute speaks of “arrangements” that “waive” mutual recovery, and an “arrangement” is clearly an understanding or agreement between parties, not a mandate or command imposed by an outside party.<sup>54</sup> *Third*, any reasonable reading of “mutual and reciprocal” recovery of costs must mean that the carrier recovers costs from the other carrier.<sup>55</sup> *Fourth*, a mandated rate of zero would constitute the imposition of a specific rate for traffic

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<sup>52</sup> *See Local Competition Order*, ¶ 1112; *see also AT&T ISP-Bound Letter* at 6-7 (“One sentence in the Local Competition Order also suggested that the ‘balanced traffic’ restriction was needed to address a legal concern: that section 252(d)(2) entitles each carrier to recover its termination costs from originating carriers, and that a LEC will be denied that opportunity under a bill-and-keep regime if it receives more traffic from another carrier than it delivers.”).

<sup>53</sup> Merriam-Webster Online Dictionary (Oct. 2008) (“*Merriam-Webster*”), at <http://www.merriam-webster.com/dictionary/waive>; *see also* Black’s Law Dictionary at 1611 (8<sup>th</sup> ed. 2004) (“*Black’s Law Dictionary*”) (“waive: 1. To abandon, renounce, or surrender (a claim, privilege, right, etc.); to give up (a claim or right) voluntarily.”).

<sup>54</sup> *Merriam-Webster*, at <http://www.merriam-webster.com/dictionary/arrangement> (“arrangement: an informal agreement or settlement...”).

<sup>55</sup> Black’s Law Dictionary at 1297 (“reciprocal: 1. Directed by each toward the other or others; Mutual”). *Merriam-Webster* also defines “mutual” as “1. directed by each toward the other or others

subject to Section 251(b)(5) and Section 252(d)(d). As explained, only the states may set specific rates.

AT&T also argues that the “additional costs” standard of Section 252(d)(2) is satisfied by establishing bill-and-keep for ISP-bound traffic. This is purportedly the case because the “additional costs” are fully paid for by carriers’ end-user charges which “permit[] a terminating carrier to recover all the costs it incurs in terminating traffic to an ISP.” *AT&T ISP-Bound Letter* at 7. But, as explained above, AT&T is grossly distorting the record: the FCC has never found that LECs’ costs of serving ISPs are fully compensated by end-user rates.

**d. The Current Rules for ISP-Bound Traffic May Not Be Sustained As “Interim” Rules.**

AT&T argues that it would be unwise to “flash-cut” to bill-and-keep immediately and implies that, even if the \$0.0007 rate were not permitted under the statute, it could be sustained as a “transitional” measure. *Id.* at 8. But the FCC has already maintained the \$0.0007 rate along with the mirroring rule on an “interim” basis for the last *seven years*. A further extension would be held to be arbitrary and capricious.<sup>56</sup>

**e. There is no Basis for Concluding that A National \$0.0007 Rate Meets The “Additional Cost” Standard of 252(d)(2).**

Level 3 argues that Sections 201 and 251(i) along with the application of the “mirroring rule” permit the FCC to allow ILECs to set the rate for ISP-bound traffic at \$0.0007 while at the same time satisfying the “additional costs” standard of Section 252(d). There is no merit to this argument.

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[and] shared in common,” at <http://www.merriam-webster.com/dictionary/mutual>. These synonymous terms clearly mean that one carrier must compensate the other for the costs imposed on its network and vice versa, not that one carrier may be compensated for its costs from a third party. Simply because costs are in fact recovered though bill and keep does not mean that this recovery is mutual or reciprocal.

<sup>56</sup> See *Competitive Telcomm. Ass’n v. FCC*, 87 F.3d 522, 532 (D.C. Cir. 1996) (“At that time, the RIC may have been a defensible compromise of two potentially conflicting objectives: encouraging an optimal mix of dedicated and common transport, and protecting smaller IXCs disadvantaged by the physical integration of AT&T and its former operating companies. Faced with considerable uncertainty about the cost properly allocable to the various transport components, the Commission apparently decided not to risk erring in a manner that might cause irreparable harm by driving smaller IXCs out of business. We need not decide, however, the question whether the interim Part 69 Rules were reasonable when adopted in 1992. *The interim period has long since expired* with no discernible progress by the FCC toward the determination of actual tandem switch cost. We conclude, therefore, that the circumstances that may have justified the Commission’s action in 1992 do not justify its continued inaction in 1994, much less in 1996.”) (emphasis added).

**i. Inclusion of \$0.0007 in Interconnection Agreements**

Central to Level 3's argument is its assertion that "where the ILEC makes an offer to terminate traffic generally at or below \$0.0007, that is strong evidence that a rate of \$0.0007 or less" is the ILEC's own estimate of its "additional cost" of terminating ISP-bound traffic. *See Level 3 Aug. 18 Letter* at 13. But simply because the ILEC has agreed to exchange all traffic at \$0.0007 subject to the mirroring rule does mean that the ILEC believes that \$0.0007 is equal to the "additional costs" of terminating ISP-bound or any other traffic. This is so for several reasons.

*First*, if an ILEC originates more traffic than it terminates, it has an incentive to agree to the lower \$0.0007 rate in order to minimize its costs. This is so regardless of whether the ILEC's cost of terminating each minute of traffic is well in excess of \$0.0007.

*Second*, the nature of complex intercarrier negotiations makes it impossible to determine the true "costs" of any particular element in that agreement. Rates for reciprocal compensation and ISP-bound traffic are typically incorporated into interconnection agreements that address many issues. *See id.* at 6. As with any intercarrier contract negotiation, ILECs and CLECs horse-trade over various terms with one side giving up a benefit in one area to gain a benefit in another.<sup>57</sup> For example, as the attached exhibit illustrates, One Communications' operating entities have agreed to a wide range of reciprocal compensation rates. *See Attachment A.* These rate differentials are not the result of differences in the costs of transport and termination. Indeed, one of One Communications' operating entities, Conversent, has two dramatically different reciprocal compensation rates in the same state (\$0.002893 and zero in Connecticut), and it did not agree to these differences because of cost differences within the state. In fact, these and other differentials in One's reciprocal compensation rates are the result of the complex analysis conducted by carriers in interconnection agreements. That analysis includes consideration of whether One is a net originator or terminator of traffic and the value of concessions offered by the ILEC in return for One agreeing to non-cost-based reciprocal compensation rates. This process obviously results in many cases in inclusion of intercarrier compensation rates in interconnection agreements that are not based on cost.

It is also worth pointing out that there are many circumstances in which commercial agreements include charges for components of the transaction that are not cost-based because the transaction as a whole is reasonable. For example, mobile wireless carriers often offer mobile devices to subscribers for "free" as part of subscription contracts. But of course the true cost of the device to the carrier is not zero. In exchange for the free phone, the subscriber agrees to pay a monthly rate that is both well above the carrier's operating costs and higher than would be the case if the carrier did not subsidize mobile devices. In this situation, neither the price of the device nor the price for the service to the customer reflects the wireless carrier's costs.

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<sup>57</sup> *See Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers*, Second Report and Order, 19 FCC Rcd 13494 ¶ 12 (2004) (describing the multi-faceted nature of interconnection agreement negotiations).



*Third*, Level 3 argues that some ILECs agree to the \$.0007 rate and some do not because some carriers' costs are higher than others.<sup>58</sup> But Level 3 does not cite to any authority in making this point. Moreover, by this argument, Level 3 admits that some carriers' costs exceed \$.0007, so, by definition, that rate cannot be cost-based.

## **ii. Uncertainty of Setting Rates for ISP-Bound Traffic**

Level 3 argues that the FCC should adopt the \$.0007 rate because of the "uncertainties" associated with calculating the "additional costs" of termination. See *id.* at 14. Level 3 asserts that TELRIC may overcompensate carriers because TELRIC switching costs "include costs not generally used for termination, such as call set-up or the capability to dip call routing databases." *Id.* Level 3 has not provided enough information to know whether this is the case. More importantly, even if Level 3 is correct, this is a reason to modify the TELRIC methodology, not to completely discard it and replace it with an arbitrarily-set rate.

## **iii. Prohibition Against Rate-Regulation in Section 252(d)(2)(B)**

Level 3 argues that, unlike TELRIC, its proposed "market-based" \$.0007 rate is consistent the requirement in Section 252(d)(2)(B) that rates may not be set pursuant to a "rate-regulation" proceeding. See *id.* But this argument is makeweight. As both the FCC and the Supreme Court in *Verizon v. FCC* determined, the ban on "rate-regulation" refers to a ban on the establishment of rates through a traditional rate-of-return or cost of service proceeding. TELRIC-based proceedings are neither.<sup>59</sup>

## **iv. Prohibition Against FCC Directly Setting Rates**

Even if Level 3 prevailed on all of the arguments above, the FCC still may not adopt a \$.0007 rate for the same reason that it may not mandate bill-and-keep (and a rate of zero). Both would involve the FCC in establishing a rate, not a rate methodology to guide states, for traffic subject to Section 251(b)(5). The fact that the ILEC can choose under the mirroring rule whether the \$.0007 rate or TELRIC applies does not transform the \$.0007 rate into a "methodology." Nor, contrary to Level 3's suggestion (see *Level 3 Aug. 18 Letter* at 15), does the a state's ratification of the FCC-mandated

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<sup>58</sup> See *Level 3 Aug. 18 Letter* at 13 ("Of course, where the ILEC believes that it would not be adequately compensated by a rate of \$.0007 or below it does not make the offer, the rate cap does not apply, and the state (or the FCC exercising its Section 201 ratemaking authority) sets the rate under Section 252(d)(2) without reference to the cap. There are many ILECs that have never opted into the \$.0007 cap for *exactly that reason.*") (emphasis added).

<sup>59</sup> See *Local Competition Order* ¶ 704 ("We find that the parenthetical '(determined without reference to a rate-of-return or other rate-based proceeding),' does not further define the type of costs that may be considered, but rather specifies a type of proceeding that may not be employed to determine the cost of interconnection and unbundled network elements."); see also *Verizon v. FCC*, 535 U.S. at 512-13.

\$.0007 cap in a state proceeding transform impermissible FCC ratemaking into state ratemaking. The fact that a state commission could establish a rate lower than \$.0007 does not alter this analysis; and an FCC mandated rate ceiling is just as impermissible as the establishment of a particular rate.

Level 3 argues that the FCC has in the past established rate caps pursuant to its price cap regulation of access services, implying that the FCC may do the same for traffic subject to 251(b)(5). *See id.* at 14-15. But there is no legal ban on direct FCC ratemaking with respect to access services as long as those services are regulated outside of Section 251(b)(5), thus rendering Level 3's argument irrelevant.

More importantly, the FCC has repeatedly found that the establishment of rate caps constitutes the establishment of rates. For example, in the *CALLS Order*, the last time the FCC set price cap levels for RBOCs, the FCC justified its plan by explaining that "the rates proposed by CALLS are reasonable."<sup>60</sup> Similarly, in the *1999 Pricing Flexibility Order*<sup>61</sup>, the FCC held that the default special access tariff prices that ILECs must continue to offer under Phase I pricing flexibility are "rates for these services." *See Pricing Flexibility Order* ¶ 24. Phase I pricing flexibility is similar to the regime in place for ISP-bound traffic and which Level 3 would like to see perpetuated; the FCC sets the "rate" at the cap while carriers and states are free to offer rates below the cap.

Crucially, in the *ISP Remand Order*, the order which contains the very rules that Level 3 believes should be extended, the FCC again found that the establishment of the \$.0007 rate cap qualified as the establishment of specific rates. For instance, the FCC explained that "the rate caps we impose are not intended to reflect the costs incurred by each carrier that delivers ISP traffic. Some carriers' costs may be higher; some are probably lower. Rather, we conclude, based upon all of the evidence in this record, that these *rates* are appropriate limits on the amounts recovered from other carriers and provide a reasonable transition from rates that have (at least until recently) typically been much higher. Carriers whose costs exceed these *rates* are (and will continue to be) able to collect additional amounts from their ISP customers." *ISP Remand Order* ¶ 7 (emphasis added). Furthermore, in describing the rate caps, the FCC noted that "[t]his interim regime affects only the intercarrier compensation (*i.e.*, the *rates*) applicable to the delivery of ISP bound traffic....[I]f a carrier argues to a state commission that traffic over the 3:1 ratio is not in fact ISP bound, [d]uring the pendency of any such proceedings, LECs remain obligated to pay the presumptive rates (reciprocal compensation rates for traffic below a 3:1 ratio, the *rates* set forth in this Order for traffic above the ratio [*i.e.*, the cap]), subject to true-up upon the conclusion of state commission proceedings." *Id.* n.149 & ¶ 79 (emphasis added). The FCC could not be clearer that it considers "caps" to be mandated rate-setting.

This view comports with common sense. If, in applying TELRIC, a state determined that a LEC's costs exceed the cap established by the FCC, it would not be permitted to set the LEC's

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<sup>60</sup> *Access Charge Reform et al.*, Sixth Report and Order *et al.*, 15 FCC Rcd 12962, ¶ 41 (2000) ("*CALLS Order*").

<sup>61</sup> *See Access Charge Reform et al.*, Fifth Report & Order and FNPRM, 14 FCC Rcd 14221 (1999) ("*Pricing Flexibility Order*").

transport and termination rates equal to the LEC's costs. It would instead be required to set the rate at the level dictated by the FCC. It is hard to see how this is anything but a "rate" set directly by the FCC.

Furthermore, Level 3's argument reduces to an absurdity. Under Level 3's logic, a "cap" of \$.0000001 is not mandated rate-setting by the FCC because states and private parties would have the "discretion" set a lower rate even though such "discretion" at such a low rate level is essentially meaningless. There is no way to determine at what point the cap would be high enough to ensure that the state had a meaningful opportunity to set rates.

Pursuant to Section 1.1206(b) of the Commission's rules, 47 C.F.R. § 1.1206(b), a copy of this notice is being filed electronically in the above-referenced dockets.

Respectfully submitted,

\_\_\_\_\_/s/\_\_\_\_\_  
\_\_\_\_\_

Thomas Jones  
Jonathan Lechter  
Willkie Farr & Gallagher LLP  
1875 K Street, N.W.  
Washington, DC 20006  
202-303-1111

Enclosures

cc: Nicholas Alexander  
Amy Bender  
Scott Bergmann  
Scott Deutchman  
Greg Orlando  
Heidi Stack  
Jeremy Marcus  
Albert Lewis  
Marcus Maher  
Randy Clarke  
Jay Atkinson  
Jennifer McKee  
Lynne Engledow  
Claude Aiken  
Nicholas Degani  
Chris Killion  
Paula Silberthau  
Matthew Warner  
Rebekah Goodheart  
Donald Stockdale

# **ATTACHMENT A**

**Reciprocal Compensation Charges Billed by One Communications Corp. Operating Entities**

	<b>Choice One</b>	<b>CTC</b>	<b>Conversent</b>	<b>Lightship</b>	<b>FiberNet</b>
<b>CT</b>	Bill and Keep	Bill and Keep	VZ is \$ 0.002893/ SNET is Bill and Keep	Bill and Keep	Bill and Keep
<b>IL</b>	\$ 0.005149				
<b>IN</b>	\$ 0.004556				
<b>MA</b>	\$ 0.008000	Bill and Keep	\$ 0.002075		
<b>MD</b>		\$ 0.0007			\$ 0.001181
<b>ME</b>	\$ 0.008114	\$ 0.0007	\$ 0.008000	\$ 0.008000	
<b>MI</b>	\$ 0.000786				
<b>NH</b>	\$ 0.008000	\$ 0.0007	\$ 0.008000	\$ 0.002670	
<b>NJ</b>		\$ 0.0007	\$ 0.002608		
<b>NY</b>	\$ 0.002893	\$ 0.0007	\$ 0.002893		
<b>OH</b>	\$ 0.004429				
<b>PA</b>	\$ 0.001823	\$ 0.0007			\$ 0.002665
<b>RI</b>	\$ 0.010000	\$ 0.0007	\$ 0.005000		
<b>VA</b>		\$ 0.0007			
<b>VT</b>		\$ 0.0007		\$ 0.008000	
<b>WI</b>	\$ 0.005273				
<b>WV</b>					\$ 0.002618